

DEFENSE CONTRACT AUDIT AGENCY  
AUDIT PROGRAM FOR DELAY/DISRUPTION PROPOSAL OR CLAIM

Contractor's Name: \_\_\_\_\_

Assignment Number: \_\_\_\_\_

Field Audit Office: \_\_\_\_\_

Date Assigned: \_\_\_\_\_

Auditor Assigned: \_\_\_\_\_  
Supervisor's Approval (Obtain  
Signature Before Starting Audit)

Note: Those steps not required should be marked "not applicable" (N/A). Portions of the audit, which are covered in other assignments (e.g. incurred cost, Disclosure Statement, and internal control audits), should be referenced at the appropriate place in this program.

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### A. PURPOSE AND SCOPE

**Purpose:** The primary purpose of the audit is to review the quantum (amount of the monetary adjustment) aspect of an equitable adjustment to determine if the proposed or claimed costs, resulting from an asserted government caused delay or disruption, are acceptable as a basis for negotiation or settlement. This audit is performed under the assumption that the allegation of entitlement may be proven valid. As part of the audit of quantum, the auditor should determine if the contractor's records show whether the contractor experienced any losses, such as increased costs or unabsorbed overhead, as a result of the asserted delay/disruption.

This program is intended to provide the proper planning, performance, and reporting on the review of a contractor's delay or disruption proposal or claim. The audit steps in the program should reflect a documented understanding between the auditor and supervisor as to the scope required to comply in an efficient and effective manner with generally accepted auditing standards and DCAA objectives. The program steps are intended as general guidance and should be tailored to determine audit risk.

**Note:** Use this audit program, APDELAY, for claims and proposals that involve an asserted government-caused delay or disruption. Use the APCLAIM2 audit program for all other proposals or claims that do not involve an alleged government delay or disruption.

**Scope:** Audit scope will generally depend on individual circumstances. In general the review should evaluate compliance with applicable acquisition regulations, CAS, and contract terms as appropriate. Related audits, systems surveys, contractor internal controls and internal reviews

should be considered when selecting specific audit steps and the extent of transaction testing to be performed. Once the preaudit analysis is performed, a transaction test program should be written based on the analysis. Additional audit steps should be developed to satisfy specific requirements of the request for audit.

The auditor should include audit steps and procedures to provide reasonable assurance of detecting errors, irregularities, abuse, or illegal acts that are material (CAM 4-702). Refer to Enclosure 5 for a listing for fraud indicators.

A requestor may ask the auditor to evaluate limited portions of contractor price adjustment submittals by means of agreed-upon procedures. Agreed-upon procedures are appropriate when objective evaluation criteria exist and the auditor and requestor reach mutual agreement on the procedures to be followed. See CAM 10-1101 and 10-1000 for further guidance.

## **B. REFERENCES**

The following references should be reviewed prior to starting the audit:

1. CAM 12-500, Equitable Price Adjustment Proposals or Claims -- Overview
2. CAM 12-600, Equitable Adjustment Proposals or Claims -- General Audit Guidance
3. CAM 12-700, Auditing Submissions Under the Changes Clause
4. CAM 12-800, Auditing Delay/Disruption Proposals or Claims
5. CAM 10-1100, Audit Reports on Equitable Adjustment Proposals or Claims
6. CAM 4-700, Responsibilities for Prevention, Detection, and Reporting of Suspected Irregularities
7. CAM 4-800, Special Reporting of Unsatisfactory Conditions
8. FAR 33, Protests, Disputes, and Appeals
9. FAR 52.233, Protests, Disputes and Appeals clauses, as applicable
10. FAR 52.236-2, Differing Site Conditions
11. FAR 52.242-14, Suspension of Work
12. FAR 52.242-15, Stop-Work Order
13. FAR 52.242-16, Stop-Work Order -- Facilities
14. FAR 52.242-17, Government Delay of Work
15. FAR 52.243, Contract clauses as applicable

## **C. AUDIT PLANNING CONSIDERATIONS**

1. A delay/ disruption proposal or claim has two elements: entitlement and quantum. Entitlement (whether the contractor has been impaired by government action and therefore has a right to a monetary adjustment) is a legal issue. However, the auditor may identify or develop information bearing on entitlement. Any meaningful observations, such as (1) failure to mitigate damages, (2) availability of replacement or substitute work during the delay period, or (3) indications that the contractor was aware

of site conditions or other causes prior to the original bid (refer to CAM 12-804d for additional items), should be conveyed to the contracting officer in the report as part of a note or in an appendix.

2. Review permanent audit files including Internal Control Audit Planning Summaries. Assess the level of the contractor's control risk and determine the nature and extent of audit effort. Review any prior equitable adjustment audit reports to ascertain the nature and extent of duplicate issues. Consider these in developing detailed steps. Determine if there were any CAS noncompliance issues outstanding during the contract performance period that may have contributed to the increased costs.
3. Review the audit request to determine the objectives of the audit, noting any specific information requested. Coordinate with the requester to gain an understanding of the nature of the proposal or claim. Determine whether there are any specific concerns or additional information that was not included in the request.
4. If the claim has been appealed to a board of contract appeals or U. S. Court of Federal Claims, a government trial attorney may request an initial audit of a claim or an "update" to an audit completed prior to the appeal. Coordinate with the trial attorney on the rules of evidence (contractor records) applicable in the circumstances. Refer to CAM 1-407 for guidance on the relationship with government legal counsel in contract disputes matters and CAM 15-500, Procedures for Actual or Potential Contract Disputes Cases.
5. If this is a construction claim, review FAR 31.105 cost principles applicable to such contracts.

#### D. PRELIMINARY AUDIT STEPS

1. Review the contractor's proposal or claim to determine if it is adequate to be audited using the attached checklist (Enclosure 1). If it is determined that the proposal or claim is inadequate for audit, coordinate with the contracting officer/trial attorney to return the proposal or claim to the contractor for supplementation prior to initiating the audit (see Part XI of Enclosure 1).
2. Prepare any audit steps necessary to satisfy specific requirements of the request for audit.
3. In planning and performing the examination, review the fraud risk indicators specific to the audit. The principal sources for the applicable fraud risk indicators are:
  - Handbook on Fraud Indicators for Contract Auditors, Section II.3. (IGDH 7600.3, APO March 31, 1993) located at [www.dodig.osd.mil/PUBS/index.html](http://www.dodig.osd.mil/PUBS/index.html),
  - CAM Figure 4-7-3, and
  - Enclosure 4

Document in working paper B any identified fraud risk indicators and your response/actions to the identified risks (either individually, or in combination). This should be done at the planning stage of the audit as well as during the audit if risk indicators are disclosed. If no risk indicators are identified, document this in working paper B.

4. Review the proposal or claim to determine if significant subcontract costs exist. Request assist audits as necessary.
5. Coordinate with the requester as soon as possible after receiving the audit request regarding the availability of technical assistance. If the

proposal includes costs for loss of efficiency or learning, determine if a technical evaluation is needed to ascertain the reasonableness of the factors used. Also request technical assistance in the evaluation of asserted days of delay, additional days of extended performance, and excess material or labor. Technical assistance may be required to determine the cost realism of the bid or negotiated cost elements (see D11).

6. Prepare a "Chronology of Significant Events" (Enclosure 2). If a list was not provided with the request for audit, contact the contracting officer and request that the list be provided per FAR 43.204(b)(5). Coordinate with the requester on the following areas as necessary as soon as possible after receipt of audit request:
  - a. Proposal or Claim. Review CAM 12-504 and the submission to differentiate between an REA proposal and a CDA claim, and if it is a routine or non-routine demand for payment. Before proceeding with the audit, contact the CO for a determination whether the submission is a proposal or claim. Refer to Enclosure 1, Steps C1 and C2. This determination is necessary before performing Step F 9.
  - b. Time Limit. If a time limit is determined to be inadequate to complete the audit (especially a major proposal or claim, sensitive review, or proposal or claim with potential for significant audit findings), request a time extension detailing the areas where work will not be completed because of the time restriction. If the extension is not granted, issue a report to the requester within the stated time period. The report should state the reasons for the denial of the time extension. In addition, coordinate with the requester to determine whether continued audit effort beyond the set due date would be

beneficial. If the requester desires continued audit effort, the audit report should also state that the audit effort is continuing and that a supplemental report will be issued.

7. Review the CO's contract files for pertinent documents such as relevant change orders, detailed field reports and job process reports.
  - a. Review all prior and current contract price adjustments for duplication of cost in the instant price adjustment.
  - b. Review all contract modifications (FAR 53.301-30, Standard Form (SF) 30, Amendment of Solicitation/Modification of Contract) for release/waiver clauses related to the specific change order or previously compensated change order proposals. The CO may have issued a supplemental agreement whereby the contractor released the government from any and all liability under the contract for further equitable adjustments relating to the same facts and circumstances giving rise to the earlier modification (See FAR 43.204).
8. Discuss the background of the proposal/dispute with the CO (and trial attorney if appropriate). Obtain an understanding of the government's position on the alleged changed condition. Document any differences between the contractor and CO. Differences concerning alleged inaccuracies in technical specifications or additional requirements may have a significant effect on labor, materials, and other submitted costs.
9. Brief the contract for the period of performance, total contract amount, and all pertinent FAR clauses or provisions. Complete a contract brief (Enclosure 3).

				Auditor's Initials and Date Completed
		<u>Staff Hours</u>	W/P	
		<u>Budget</u>	<u>Actual</u>	<u>Ref.</u>
<p>a. For manufacturing/supply contracts, review First Article Testing provisions in the contract, FAR 52.209-4(c), that may limit the costs for retests to be borne by the contractor.</p> <p>b. For construction contracts, determine if the contract provides for liquidated damages payable to the government for each day's unexcused delay beyond a predetermined completion date. Such a clause may appear in any contract, by agreement of the parties. It is important to remember that the clause was placed in the contract to protect against delays, such as material outages, which are within the contractor's control, but are not government caused.</p> <p>10. Determine whether an audit of the initial pricing proposal was performed. If an audit was performed, review the proposal and the audit report for any information that may impact the claim.</p> <p>11. Review initial pricing or bid data to determine if the contractor may have underbid the original contract, which would impact the labor, material, or other costs submitted (reference FAR 3.501). If no audit was conducted on the initial pricing proposal, request and review the contractor's support data related to the initial pricing proposal or bid.</p> <p>a. Compare the bid or negotiated cost elements and actual cost data, exclusive of that related to the delay to determine a possible loss on the contract. Technical assistance may be required to evaluate any significant differences in labor hours or material quantity costs. Claimed cost elements unrelated to the delay that were not included in the bid may indicate underbidding.</p>				



	<u>Staff Hours</u>		<u>W/P Ref.</u>	<u>Auditor's Initials and Date Completed</u>
	<u>Budget</u>	<u>Actual</u>		
<p>b. Question costs unrelated to the delay including those underestimated in the bid. Provide comments on the contractor's profit or loss position in the audit report.</p> <p>12. Review FAO files to determine if a DCAAF 2000.0 has been filed that relates to the subject matter of the proposal or claim. If it has, notify the appropriate investigative agency or DOJ attorney of the proposal or claim. Notify the contracting officer of the DCAAF 2000.0.</p> <p>13. If the contractor is classified as non-major (where ICAPS have not been completed) and if the evidential matter to be obtained during the audit is highly dependent on computerized information systems, document the audit work performed that supports reliance on the computer-based evidential matter. If the contractor's controls related to these systems have not been specifically/adequately tested in other audits, the auditor needs to either (1) develop, document, and reference in B-2 the procedures/tests in this audit that will support reliance on the evidential matter or (2) qualify the audit in accordance with CAM 10-210.4a and 10-1104.4a.</p>				

#### **E. ENTRANCE CONFERENCE**

1. Arrange an entrance conference with the contractor personnel responsible for the proposal or claim. Make sufficient inquiries to fully understand the basis of the proposal or claim and the issues involved.
2. Make sufficient inquiries to fully understand the contractor's position regarding the nature of the delay/disruption and the extent of alleged government responsibility. Discuss these items with the Contracting Officer. Differences concerning alleged number of delay days may

	<u>Staff Hours</u>		<u>W/P</u>	<u>Auditor's</u>
	<u>Budget</u>	<u>Actual</u>	<u>Ref.</u>	<u>Initials</u>
				<u>and Date</u>
				<u>Completed</u>
have a significant effect on labor, materials, and other submitted costs.				
3. Make inquiries to fully understand the methodology used to develop the price adjustment. Determine if different methodologies were used for different cost elements.				
4. Obtain additional supporting data including budgets and actuals for indirect costs (including allocation bases and fixed and variable costs), direct costs, labor hours and costs, material costs, and subcontracts, and audited financial statements and tax returns for the entire performance period of the contract.				
5. If external legal or financial consultants prepared the proposal or claim, obtain a copy of their working papers that support the proposal or claim. Costs incurred for proposal or claim preparation should be identified separately from other claimed costs to determine their allowability (see Step F. 9).				
6. Review the contractor's correspondence and contract files for relevant documents. Obtain a list of all outstanding and recently settled claims adjustments on other contracts that relate to the period of performance of the subject contract.				

## **F. DETAILED AUDIT STEPS**

1. Contractor's Proposal or Claim Submission.
  - a. If the contractor's proposal or claim/support was initially determined to be adequate for audit as a result of applying preliminary audit step D.1., but is subsequently determined to be inadequate during field work (e.g. referenced supporting documentation is inadequate or unavailable), discuss what additional data is needed with the contractor.

<u>Staff Hours</u>		<u>W/P Ref.</u>	<u>Auditor's Initials and Date Completed</u>
<u>Budget</u>	<u>Actual</u>		

If such data is not reasonably available, follow the procedures in Part XI of Enclosure 1.

- b. Perform mathematical verification of the proposal or claim and supporting data.
  - c. Coordinate with the CO to determine what clause(s) the contractor based its recovery on and if the submission complies with the conditions of the clause(s). For example, if the contractor claims profit, is a profit factor permitted by the clause used as a basis for the price adjustments (See CAM 12-502 and 12-802.7)? If not, provide this information in the audit report.
2. Review the prime contractor's subcontract files.
- a. Follow up with cognizant FAOs for subcontractors identified in Step D. 4 to assure timely issuance of assist reports for incorporation in the audit report. If there will be a delay in the issuance of the assist audit report, coordinate with the CO to determine if the results can be forwarded directly to the CO after issuance of the prime report.
  - b. Forward any pertinent data such as lien releases, correspondence and the like to the subcontract auditor. Offer to provide any additional supporting data the assist auditor may require.
  - c. Review the prime contractor's correspondence file for legal documents related to subcontractors. A review of the files may disclose that the prime contractor is holding the subcontractor liable for increased costs as a result of changed conditions caused by the subcontractor, or that the subcontractor waived its rights at some point.

				Auditor's Initials and Date Completed
		<u>Staff Hours</u>	W/P	
		<u>Budget</u>	<u>Actual</u>	<u>Ref.</u>
d.	Determine if the prime contractor has recorded a liability in the accounting records for the subcontractor's claim. While a failure to do so does not preclude recovery, it is an indicator of the prime contractor's belief in the validity of the subcontractor's claim.			
e.	For construction contracts, determine if any of the original subcontractors defaulted. If there were subcontractor defaults, determine if the prime received or will receive payments from the original subcontractor's bonding company (surety). Question any payments from the bonding company that are related to claimed costs.			
3.	Subcontract Audit.			
a.	Advise the subcontractor that the audit report may be made available to the prime contractor or upper-tier subcontractor and that the audit report will indicate the extent to which the subcontractor agrees to disclosure of the results.			
b.	Obtain the subcontractor's consent for release of the audit report or reason(s) for not authorizing release. If there are restrictions to the release of data to the prime, ask the CO whether the audit should be continued.			
c.	Coordinate with the prime auditor on due date and other items of mutual concern.			
d.	Brief the contract between the prime and the subcontractor. Determine if an exculpatory clause limits the prime contractor's liability to the subcontract price. If such a clause is included, determine if the prime contractor's right to recover damages is limited. A deviations and substitutions clause may limit the liability of the prime for any substitutions			

or deviations not approved by the government.

#### 4. Internal Documentation.

- a. Ascertain the operations or departments affected by the delay and the extent of any related work rescheduling or rephasing. Review backlog or internal job log documents that include information on commercial as well as government jobs. Obtain a description of the numbering system used to distinguish one job from another job. This information can assist in identifying replacement contract(s) or accelerated work on other contracts. (Refer to Step 11 c (7)).
- b. Review all time-phased work/production schedules of the entire contract performance period as contemplated before the delay occurred, and a schedule of work as actually performed, to assist in determining the extent and perhaps the cause of the delay. For example, the contractor may have adjusted the work schedule for reasons unrelated to the proposal or claim, or labor efficiency may have been reduced due to weather, fire, strike, or other causes.
- c. Also review all time phased work/production schedules from key subcontractors, whether or not they are requesting unabsorbed overhead. Such information can provide additional information useful in evaluating the prime's claim and could show inconsistencies between the subcontractor's and prime contractor's representations.
- d. Review all contemporaneous revenue projections by contract on a plant-wide basis where the time period for such projections encompasses at least in part, the time period encompassed by the entire performance of

the contract including the period of delay. If total actual revenues match or are greater than planned revenues or certain contracts have higher actual revenues than planned, this may indicate that the contractor accelerated the work on certain contracts or substituted new work for the work on the delayed contract.

#### 5. CAS and FAR Implications.

- a. Determine if the contract contains the CAS clause before proceeding with this section. Delay and disruption claims commonly arise under fixed-price contracts and frequently under sealed-bid contracts or contracts otherwise exempt from CAS or FAR Part 31.
- b. Refer to the contractor's Disclosure Statement (if any) in effect during the period of incurrence of proposed or claimed costs including the proposal or claim and results of prior reviews. Ascertain that accounting for significant cost elements in the proposal or claim is consistent with established/disclosed practices and complies with FAR Part 31 and the Cost Accounting Standards if applicable. Delay or disruption proposals or claims may include as direct charges, costs which would have been indirect. In such cases, the auditor should document in the audit working papers the justification for the departure from established cost accounting practices.
- c. Refer to the DMIS and CAS Compliance Testing Reports in the permanent file or planning file. A CAS compliance review should be accomplished, as needed and documented for applicable standards (see standard audit program for such reviews).
- d. Coordinate with your supervisor for possible audit extension and issuance of separate

assignment number for a noncompliance report if positive noncompliance situations are indicated. Materiality should be considered prior to initiating a separate noncompliance report. Refer to CAM 8-302.7.

- e. Determine if the contract contains the Pricing Adjustments clause (DFARS 252.243-7001) that requires costs to be in accordance with FAR Part 31.

#### 6. Delay and Extension Days

Request the contractor to provide documentation in support of the proposed number of delay or disruption days and the number of extension days (CAM 12.804.4). Coordinate the number and dates of the delay and extension days submitted with the contracting officer/trial attorney. This information is frequently used in calculations of labor, material, and unabsorbed overhead costs. In addition, the contractor is precluded from recovering the same cost more than once for overlapping delays. Incorporate the results of the technical evaluation.

#### 7. Transaction Testing Program

Draft a transaction testing program to determine the cause and the allowability and allocability of proposed or claimed costs as appropriate for the following areas:

- a. Labor
  - (1) Verify maintenance or standby labor hours to timesheets or other supporting documentation and labor distribution reports. Determine if the standby labor was diverted to other contracts or other production usage and that the decision to retain standby labor was reasonable in

the circumstances. For instance if other work was available, determine why "idle labor" was not employed on such work.

- (2) Determine if the claimed direct labor is recorded on the contractor's accounting records separate from the indirect labor, supported by time sheets or other accounting records. Review the basis for any estimates.
- (3) Determine if any of the submitted costs are due to (i) a change in scope or specifications, (ii) the normal increase that often occurs as a contract "tails off", or (iii) other factors unrelated to the delay. Technical assistance may be required to make this determination.
- (4) Review any communications or meetings between the contractor and any or all labor unions, related to the delayed contract. Review union agreements covering the delayed period to understand any possible adverse impact in the event of a decrease in work.
- (5) Determine if the contractor laid-off employees as a result of the alleged government caused delay or disruption. Review relevant documentation (time sheets) as to the date of discharge and possible recall.

b. Material

- (1) Price variance: Trace amounts claimed to purchase invoices, since a contractor frequently executes firm commitments for major material requirements at the time the contract or modification is signed to protect against cost growth.



- (2) Quantity variance: Determine if the change in number of items used was the result of loss due to scrap and spoilage, deterioration over time, theft, inadequacy of initial estimate or other causes, any of which may or may not arise from government actions. Technical assistance may be required.
- (3) Evaluate any changes in make-or-buy decisions subsequent to contract award to determine their impact on costs not caused by the delay. Also consider changes to proposed manufacturing processes that result in increased costs unrelated to the subject delay or disruption.

c. Indirect Costs

- (1) Determine if indirect expenses allocated to direct costs associated with delay are allowable and in accordance with the contractor's cost accounting system.
- (2) Determine if indirect expenses reclassified as direct are appropriate to the circumstances if they are not in accordance with the cost accounting system.
- (3) Analyze indirect costs associated with "standby" direct costs to determine that the underlying causal-beneficial relationship is still valid. For example, "standby" direct labor may require no supervision and the related supervisory labor may not be in a standby status. If such a case exists, the indirect costs applicable to standby labor should be adjusted accordingly.

- (4) Determine that costs are not subject to duplicate recovery (both as direct costs and through an overhead rate) in the same time period. Contractors sometimes include as a direct charge certain expenses normally included in overhead when work on a contract ceases during a delay. Such items as occupancy costs, insurance, equipment rental or depreciation may continue, and should be treated as ODC when this happens.
- (5) Determine if these costs have been removed from the overhead pool for final rate determination or any other existing contractor claims. Review audit files for prior claims of indirect costs as ODC.

#### 8. Transaction Testing Program Audit Steps

Perform the audit steps developed in the transaction testing program developed at step F. 7.

#### 9. Proposal or Claim Preparation Costs

- a. Claim prosecution costs incurred after the submission of the claim to the CO are unallowable even if incurred in support of negotiations or alternative disputes resolution (ADR) processes (see CAM 12-606b). Determine if claimed preparation and support costs are factually related to the submission of the claim. Such costs are unallowable per FAR 31.205-47(f). Review invoices and other documents sufficient to ascertain the nature and scope of the services provided.
- b. Determine if proposal preparation costs are reasonable (FAR 31.205-33) in relation to services rendered. Review the contract(s)

with consultants. If the fee is contingent upon recovery from the government, question the costs.

- c. Ascertain the contractor's practices for charging equitable adjustment proposal preparation costs. The courts have ruled that allowable equitable adjustment proposal preparation costs are generally not reimbursable as a direct cost. However, such preparation costs may be a direct charge if consistent with the contractor's disclosed accounting practices.

#### 10. Construction Contracts

- a. Review the job site diary, as important information not available in the accounting records may be available here. Such information may include extent of work performed, status of employees during delay periods and types and dates of equipment usage. Discuss data found in the records with those employees responsible for the records. Compare the data with that provided in the proposal or claim to determine if there are any discrepancies. Determine the basis for any discrepancies.
- b. Review the contractor's Davis-Bacon Act certified payroll record reports submitted weekly to the government for the period under review. These reports are usually submitted on Dept. of Labor Form WH-347 (a copy of the form is included in FAR 53.303-347). The reports contain weekly payroll data: employee name, work classification, social security number, pay rate, pay period, hours worked per day and for the total week and total pay applicable. Determine if the records indicate whether the employees working on the job prior to the delay continued to work on the job full time

or part time during the period of delay. Verify employees' pay rates on the form to the contractor's payroll records, paid checks, and submitted costs.

- c. If the proposal or claim includes costs of construction equipment, review the submitted costs based on the allowability requirements set forth in FAR 31.105(d)(2).

(1) Determine the contractor's basis for claimed equipment costs, actual equipment costs or predetermined rates.

(2) Actual cost data:

(a) Trace claimed actual equipment costs to the contractor's books and records.

(b) Determine if cost data is available for each piece of equipment claimed or groups of a similar series or serial equipment (FAR 31.105(d)(2)(i)(A)). If the data is available, the FAR requires that the actual data should be used and not predetermined rates. If the data is not available, actual cost data may not be used.

(c) If the equipment was idle or on standby during the alleged delay, question any claimed operating costs, such as gas, fuel, and operators' costs.

(d) Analyze the accounting assumptions used in the computation of actual equipment costs, such as equipment life and year entered into service. This data should be reconciled to other job records and company-wide financial accounting data. Verify

any salvage values used in the equipment costs calculations.

- (e) Determine if the equipment costs are claimed in accordance with the contractor's normal capitalization policies. Items not customarily capitalized should be omitted from the contractor's equipment costs. If the contractor normally expenses the costs of wheelbarrows or small tools, these should be omitted from equipment calculations.

(3) Predetermined rates:

- (a) Determine if the contractor met the FAR criteria permitting the use of the schedules (see (2)(b)). Determine if the contractor's accounting system is capable of identifying the equipment costs based on the FAR criteria. If the data can be obtained, the rate schedules should not be used.
- (b) Determine if the contract specified predetermined rate schedules to compute equipment costs. If a schedule is not mandated, request technical assistance on the choice of an appropriate rate schedule. If the contractor used a schedule other than the one mandated in the contract, determine the reason for the deviation.
- (c) Verify the contractor's rate computations to the predetermined rate schedule used to compute the equipment costs.

- (d) Review other claimed direct and indirect costs to determine if the costs of equipment claimed are included. Remove any claimed equipment costs that are duplicative
- (e) If claimed equipment costs included costs contained in non-equipment cost categories at the time of the bid or in other accounting records, determine the basis for reclassifications. Any claimed equipment costs not bid or unrelated to the subject delay or disruption should be disallowed (see CAM 12-802.7b).
- (f) Report any evidence that the claimed equipment was used for other work during the alleged standby period.

d. Job Site/Field Overhead

- (1) Evaluate the proposed or claimed job site/field overhead costs to determine if home office overhead costs are included. Question any home office costs included in the job site/field overhead costs.
- (2) Determine whether the allocation method the contractor uses for changes that increase the performance period is consistent with the contractor's established accounting practice and applied for all contracts. If the allocation method is not consistent with the established accounting practice, recompute the overhead using the consistent method. Compare this amount with the proposed or claimed amount and question any differences (CAM 12-802.4b).

e. Bonding Costs:

- (1) Brief the contract for the bonding requirements clause (FAR 52.228-15).
- (2) Verify the computation of bonding costs. Determine if the contractor's computation is based on the correct rate for the appropriate level of contract revenues.
- (3) Determine the total bonding costs included in the original contract price, modifications and subject claim. Compare this amount with incurred costs or future liability. Question the difference.

11. Unabsorbed Overhead and Audit of the Eichleay Formula

- a. Determine the formula or method the contractor applied to compute the claim for recovery of unabsorbed overhead. If the contractor applied a formula other than the basic Eichleay formula (see Enclosure 5) such as the modified Eichleay, determine the basis for its use as opposed to the basic Eichleay formula.
- b. Check the mathematical accuracy and support of the contractor's computations used in the methodology or formula. Review all working papers that support the contractor's computations. If the contractor hired consultants to prepare the claim, request all working papers that support the consultants' work product. Reconcile the contractor's data to incurred cost records and other documents as appropriate.

c. Audit of Eichleay formula damages :

- (1) Examine the Eichleay formula billings/allocation ratio components (Refer to Enclosure 5).
  - (a) Determine if the contract billings (revenues), total billings (revenues), total fixed overhead and days of performance are for the same time interval from the date of contract award to the completion date. Billings are not progress payments or public voucher payments (see CAM 12-804.2).
  - (b) Determine if the billings data (contract revenue) used in the allocation ratio are accurate and appropriate.
    - i. Determine if the contractor uses an allocation base other than contract billings (such as contract labor/total labor). If so, compare this ratio with the established Eichleay formula allocation ratio and contract billings/total contract billings.
    - ii. Recompute the Eichleay formula using the billings allocation ratio unless the impact of a different measurement allocation base is immaterial or the contractor can demonstrate that the Eichleay formula billings allocation ratio would lead to inequitable results.
    - iii. If the contract has not been completed, determine if the contract billings and total contract billings (Step 1 of the formula in Enclosure 5) include estimates to complete.



				Auditor's Initials and Date
		<u>Staff Hours</u>	W/P	
		<u>Budget</u> <u>Actual</u>	<u>Ref.</u>	<u>Completed</u>

Evaluate the basis and reasonableness of the estimates.

- (c) Review the contractor's method for recognizing revenue (billings) to determine if the method results in an inequitable allocation of unabsorbed overhead (Step 1 of the formula in Enclosure 5).
  - i. Percentage-of-completion method.  
Evaluate the assumptions used to measure the extent of progress towards completion.
  - ii. If completion is overstated or understated, adjust the billings (revenues) whether in the numerator or denominator of the formula to prevent over or under recovery of unabsorbed overhead..
- (2) Analyze the overhead thoroughly to remove all variable overhead costs. If semi-variable costs are included, remove the variable portion (CAM 12-804.3). Ensure that all unallowable costs are removed from the overhead.
- (3) Determine if the "delay days" used in the contractor's Eichleay formula computations represent only the number of days that the performance of the contract was extended beyond the original or previously revised completion date because of a government caused delay or suspension. Technical assistance may be required. Question any days that are not related to the extended performance period caused by the government delay or suspension (CAM 12-804.4).

- (4) Recompute the Eichleay formula using the results of Steps 11c(1)-(3) if required. Refer to Enclosure 5.
- (5) Compare the contractor's Eichleay formula computations with the results of Step 11c(4). Question the difference between the contractor's computation and the results of audit. Use the worksheet in Enclosure 6.
- (6) Credits: Determine if the audit computed Eichleay damages (Step 11c(4)) include:
  - (a) Fixed overhead proposed or reimbursed that was applied to direct costs in the submission, and any new change order work or out-of-sequence work performed on the delayed or suspended contract during the delay and extension periods.
  - (b) Identify the out-of sequence work or change order work: date and number of the change order/modification, type of work, dollar amount, and date(s) work performed.
  - (c) Calculate the credit for out-of-sequence work and new change order work on the delayed or suspended contract using Steps 1-3 in Enclosure 7. Question the costs as a credit to the Eichleay formula. Add the questioned costs to the worksheet in Enclosure 6 as a "Credit."
  - (d) Credit the Eichleay formula results for any fixed overhead that the prime contractor applied to a subcontractor's proposed or claimed unabsorbed

overhead. Add the questioned costs to the worksheet in Enclosure 6 as a "Credit."

(7) Assess the impact of replacement work or accelerated work on other contracts:

(a) Review contractor records for evidence of replacement contract(s) or accelerated work. (CAM 12-805.4a-c) Indicators include:

i. Labor registers that show personnel from the delay contract were assigned to other contracts during the delay period.

ii. Fixed overhead rates, during the delay period and extended performance period that decreased or were unchanged.

iii. New contracts for work not normally performed by the contractor added during the delay and extension periods.

(b) Identify replacement contracts or accelerated work with:

i. Replacement contract: date of award, contract number, performance period, amount of contract, the type of effort, duration or size and location (CAM 12-805.4b).

ii. Accelerated work: date of award, contract number, a schedule of the work as planned and as performed, total amount of the contract and the type of work. (CAM 12-805.4c)

- (c) Compute the impact of the replacement contract and accelerated work using Steps 1-9 in Enclosure 7.
- (d) Add the questioned costs to the presentation worksheet in Enclosure 6. The questioned costs are the difference between the Eichleay formula as audited and the computed impact of replacement work or accelerated work, as shown in Step 9 in Enclosure 7.

## 12. Total or Modified Cost Method

If the contractor computed any element(s) of the proposal or claim using the total cost or modified total cost method, perform the following steps to determine if the contractor meets the criteria for acceptable use of the method. These steps should be performed in addition to any of the foregoing applicable steps. Determine if the contractor's proposal or claim meets the following criteria:

- a. Impossible to determine actual related increased costs.
  - (1) Review the contractor's accounting system to determine the capability and requirements to separately account for increased costs caused by the asserted change(s).
  - (2) Determine if the contract included the Change Order Accounting Clause (FAR 52.243-6). Determine if the CO issued any directives requiring the contractor to establish separate cost accounts for activities related to changed work and if the contractor complied with the directive.

- (3) If the contractor is CAS covered, review the disclosure statement for statements regarding the capability of the accounting system to segregate costs when necessary.

b. Bid is realistic.

- (1) Compare the bid with Request for Proposal (RFP) requirements. Determine if any significant elements were omitted from the bid but included in the submitted costs.
- (2) Compare the contractor's bid with other contractors' bids for the same acquisition, if available from the CO.
- (3) Compare the proposed price to recent historical data of similar work. If the bid is significantly less, determine why.
- (4) Compare the contractor's bid delivery schedule with those of unsuccessful bidders. Determine the reasons for significant differences.
- (5) Compare bid cost elements to incurred cost elements. Examine those elements where the bid and the incurred costs are significantly different. Determine the reason for the difference.
- (6) Review prior audit reports on the contractor's estimating system for deficiencies that may have impacted the reasonableness of the bid.

c. Incurred costs were reasonable.

- (1) Reconcile the claimed costs to the contractor's books and records. Determine if the incurred costs were

allocable, allowable and reasonable in nature. Question those costs proposed or claimed that were not incurred or would not be incurred.

- (2) Obtain technical assistance to determine the cost realism of the estimate to complete if the contract is not yet complete.
- (3) Determine if the contractor used estimates based on incurred costs. Any add-on factors to incurred costs or estimated costs should be logical and reasonable in the circumstances.
- (4) Evaluate changed methodologies from the bid to the incurred costs. Determine if the contractor changed the labor mix or revised the make-or buy decisions. Determine the impact on submitted increased costs.

d. Government is clearly responsible.

- (1) Review the contract budgets for the period of performance and the contractor's policies and procedures for comparing actual performance to the budget. Identify and analyze variances the contractor should have identified as work was accomplished. Gather information on contractor caused increased costs and increased costs due to alleged changed work.
- (2) Determine if the contractor implemented any accounting changes having impacts that were not considered in the claim.
- (3) Determine if the contractor recognized any increased costs attributable to its

				Auditor's Initials and Date Completed
		<u>Staff Hours</u>	W/P	
		<u>Budget</u> <u>Actual</u>	<u>Ref.</u>	

own mismanagement in scheduling or material procurement.

- (4) Review correspondence between the prime contractor and the subcontractor(s) for indications of subcontractor failure to perform according to schedule or other issues that would cause increased subcontract costs.
- (5) Determine if there were extraordinary equipment repairs or delayed material ordering or deliveries that were charged to the contract and not the responsibility of the government.
- (6) Review increased incurred overhead costs that may have been caused by loss of planned contract awards, contractor-caused delays, or contract terminations that are not the responsibility of the government.
- (7) Determine if there were higher than normal material scrap costs that may indicate contractor caused cost growth.
- (8) Review increased incurred overhead costs that may have been caused by loss of planned contract awards, contractor-caused delays, or contract termination that were not the responsibility of the government.
- (9) Determine if the prime contractor proposed or claimed hours that were actually performed by a subcontractor. Determine if the subcontract was firm-fixed-price and if there was a change to a cost reimbursement contract. If there was no change, there is no liability to the government.

- e. Based on the results of performing the previous steps, determine if proposed or claimed costs are acceptable as a basis for negotiation or settlement because they meet the four criteria for applying the total cost method.
- f. **Modified Total Cost Method**  
Perform the relevant steps above. Determine if the adjusted costs were accurate and complete.

## **G. CONCLUDING AUDIT STEPS**

1. Summarize audit findings on lead schedules. Include narrative comments, which concisely describe the contractor's basis for proposed or claimed costs, questioned costs and basis of determination.
2. Review technical reports and translate findings into dollars. Any reservations by the auditor in regard to scope, basis for conclusions, etc., included in the technical reviews should be coordinated with government technical personnel before incorporation of the technical report into the audit report (CAM 4-1000).
3. Complete other audit work papers.
4. Determine if any fraud indicators are present (Enclosure 4). Review findings with supervisor. Take actions indicated by CAM 4-700 or 4-800.
5. Discuss audit findings with supervisor and FAO claims technical specialist (if available).
6. Arrange and conduct an exit conference with contractor representatives in accordance with procedures specified in CAM 4-300. For claims appealed to the BCA, coordinate with the trial attorney prior to conducting an exit conference.



	<u>Staff Hours</u>		<u>W/P</u>	<u>Auditor's</u>
	<u>Budget</u>	<u>Actual</u>	<u>Ref.</u>	<u>Initials</u>
				<u>and Date</u>
				<u>Completed</u>
7. Draft audit report using the guidance in CAM 10-1100. Include contractor responses and where appropriate the auditor's rebuttal.				
8. Update permanent files as necessary (including Internal Control Audit Planning Summaries (ICAPS)).				
9. Determine the need for issuance of other related reports (e.g., CAS noncompliance report and/or flash internal controls deficiency report).				
10. The supervisory auditor should validate dollars examined and costs questioned in the DMIS Audit Disposition Form to assure compliance with Agency instructions.				
•				
11. Closing actions should be performed in accordance with FAO procedures. These procedures may require either auditors or administrative personnel to perform various closing steps. Completion of these closing actions should be documented in the working papers and should include:				
a. If the audit report has been electronically transmitted to the customer, file the signed original report in the audit working paper package. Otherwise, file a copy of the signed report.				
b. Include a printed copy of the final draft audit report containing the supervisory auditor's initials and date on the top page, cross-referenced to the working papers, in the working paper package. The final draft report should include all substantive changes made to the original draft, with cross-referencing updated as necessary. It				

	<u>Staff Hours</u>		<u>W/P</u>	Auditor's
	<u>Budget</u>	<u>Actual</u>	<u>Ref.</u>	Initials
				and Date
				<u>Completed</u>
<p>should differ from the final report only due to minor administrative changes (spelling, format, etc.) made during final processing.</p>				
<p>c. Include an electronic version of the acknowledgement letter in the audit working paper package.</p>				
<p>d. Include hardcopy printouts of the Administrative and Audit Working Papers indexes, including the supplemental listing of electronic files, in the working paper package.</p>				
<p>e. Ensure all working paper files are "read only" and, if necessary, compressed for final storage. Generally, current Agency software should be used to automatically modify all electronic files for storage.</p>				
<p>f. Two complete sets of electronic working papers must be prepared. The "original" set should be stored in the working paper package. The "archive" set is to be stored separately from the working paper package on removable media such as CD-ROM or diskette. If there will be a short-term need to access the working papers, a third, or "working" set should be stored so as to be available for reference, generally on the LAN. This set should be deleted when no longer needed.</p>				
<p>g. Verify that electronic files stored on removable media are not corrupted and can be unarchived.</p>				
<p>h. Securely enclose the "original" set of electronic files in the working paper package.</p>				

**SCREENING CHECKLIST  
EQUITABLE ADJUSTMENT PROPOSAL OR CLAIM**

Contractor: \_\_\_\_\_

Assignment No.: \_\_\_\_\_

Auditor's Name: \_\_\_\_\_ Date: \_\_\_\_\_

Reviewer's Name: \_\_\_\_\_ Date: \_\_\_\_\_

**I. Background**

The following screening checklist is provided to assist in determining whether the contractor's equitable adjustment proposal or claim is adequate for audit. Only if the proposal or claim is submitted in substantially the same format and containing the same data as required in a completed Table 15-2 (FAR 15-408(m)) is it considered adequate for audit. The checklist should be used prior to beginning the audit. See CAM 12-503 for further guidance on audit adequacy of equitable adjustment proposals or claims.

None of the contract clauses that authorize equitable adjustments require a contractor to submit any data in support of its request for adjustment. Additionally, the FAR coverage of claims does not require a contractor to disclose any data in support of its claim. Further, the Court of Appeals for the Federal Circuit and the ASBCA have held that a contractor does not have to disclose any data to support the quantum aspect of a claim. Thus, unless there is a specific term in the contract that requires a contractor to disclose data relating to a request for equitable adjustment or claim, the only regulatory or statutory requirement in this regard is found in TINA and FAR Part 15. However, these requirements apply only to requests for equitable adjustment if the request exceeds the TINA threshold and the contracting officer requires the submission of cost or pricing data. Despite this, it is usually in the contractor's best interest to disclose adequate data to support its request for equitable adjustment or claim if the contractor wants to be paid quickly. However, the manner of such a disclosure and the format in which the data is presented is within the discretion of the contractor. Nonetheless, auditors should not start the audit without obtaining adequate supporting data. Only if the contracting officer insists that the audit be performed on the inadequate data provided with the proposal or claim, should the audit proceed after following the guidance in CAM 12-503.

The reviews of equitable adjustment proposals or claims have historically been high risk audits resulting in large amounts of questionable costs largely due to inadequate supporting data. If during the screening process, the auditor finds reasonable suspicion of fraud, corruption, or unlawful activity, the auditor should refer to CAM 4-702, which explains the auditor's responsibilities in these areas. Specific fraud indicators that the auditor may encounter during the proposal or claim audit are discussed in Enclosure 4 of the standard audit program for a delay/disruption proposal or claim.

## II. Screening for Audit Adequacy of Proposal or Claim

The following checklist is intended to assist in screening the contractor's proposal or claim, before commencing the audit to conserve audit resources and to identify inadequately supported proposals or claims. To answer some of the questions, the auditor will need to have knowledge of the contractor or make additional inquiries of the contractor, e.g., question 4 below. Questions coded with a "C" indicate that they are critical to the acceptability of the proposal or claim. A "no" response to any one of them will often result in the auditor recommending that the proposal or claim be rejected or denied by the Contracting Officer (CO). Questions coded with an "S" are critical if related proposed or claimed costs are significant.

COMMENT  
YES NO NA REFERENCE

## III. General Steps:

C1. Did the contractor provide a signed certificate for the claim as required by FAR 52.233-1 (above \$100,000)? (If no, coordinate with the requester and the contractor to obtain timely certification. If not obtained, the CO should be advised to return the claim to the contractor.)

C2. For proposals, did the contractor provide a signed certification for the request as required by DFARS 252.243-7002 (if applicable), if the request is above the simplified acquisition threshold (\$100,000)? If the contractor is required to submit cost or pricing data, did the contractor submit the data in conformity with Table 15-2 of FAR 15.408(m).

C3. Did the contractor identify the factual data available in the accounting records to support the proposal or claim and is access available to all relevant factual data? (Inquire about job site diaries, equipment utilization records, project status reports and the like.)

C4. Are the contractor's accounting books and records available to support the proposal or claim?

C5. If the contractor's accounting system does not adequately identify and segregate costs by project and contract, has the contractor summarized the incurred costs from pertinent source documents to fully disclose the actual costs applicable to the contract and the proposal or claim?

S6. Is each cost element of the proposal or claim adequately supported by relevant and factual cost data? (The data needs to be either included in the proposal or claim or specifically identified and referenced.)

C7. Did the contractor adequately explain the causes for the proposed or claimed increased costs and the time periods involved?

C8. For a delay proposal or claim, did the contractor identify and support the delay period?

C9. Is access available to the original bid? (This is particularly important when the contractor's proposal or claim is based on the difference between bid costs versus actual costs, either in total or by element of cost. See CAM 12.704 Total Cost Method.)

#### IV. Direct Labor:

S10. Did the contractor provide support for the causal relationship between the proposed or claimed labor hours and the alleged delay or disruption?

S11. Did the contractor include or specifically identify the data to adequately support the proposed or claimed hours and hourly rates for each direct labor category? (Key source documents include: completed timecards; payroll records; job site diaries, if a construction contract; and personnel records.)

S12. If an improvement curve is used to support a proposed or claimed loss of efficiency or learning, is it adequately supported by past performance, industry standards, or other acceptable basis?

S13. Does the proposal or claim give consideration to any changes affecting direct labor such as changes in make-or-buy decisions, production methods, and labor mix made subsequent to contract award?

- Is the impact of the changes on the proposal or claim adequately supported?

V. Materials:

S14. Did the contractor provide support for the causal relationship between the proposed or claimed material costs and the alleged delay or disruption?

S15. Did the contractor include or specifically identify the data to adequately support the claimed material costs? (Key source documents include: requisitions; purchase orders; invoices; receiving reports; paid vouchers; canceled checks; records of excessive scrap possibly due to faulty specifications; bills of materials; and drawings.)

S16. Does the proposal or claim give consideration to any changes affecting material costs such as changes in make-or-buy decisions and production methods made subsequent to contract award?

- Is the impact of the changes on the proposal or claim adequately supported?

VI. Subcontracts:

S17. If the proposal or claim includes subcontract costs, did the contractor obtain and analyze an adequate subcontract proposal or claim and include the results of that analysis in the proposal or claim?

S18. If required to be certified, was the prime claim certified? (See FAR 52.233-1, if above \$100,000.) The prime contractor must certify claims filed by the subcontractor .

VII. Indirect Expenses:

S19. Did the contractor show how the indirect expense rates were calculated and applied? The support for the indirect rates should consist of cost breakdowns, trends, and budgetary data.

S20. Did the contractor identify and exclude the unallowable indirect expenses from the indirect expense pools?

S21. Did the contractor demonstrate the causal/beneficial relationship between indirect expenses and the allocation base for such unusual items as standby labor?

VIII. Unabsorbed Overhead:

S22. If the Eichleay method was used to compute unabsorbed overhead, did the contractor provide adequate support for the formula components (e.g. showing the source of "Contract Billings," "Total billings" and "Days of Performance")? If some other method was used, did the contractor provide an adequate explanation of how the method is applied? Did the contractor provide adequate support for the calculations?

IX. Other Direct Costs:

S23. Did the contractor include or specifically identify the data to adequately support claimed other direct costs (e.g., travel costs, overtime premium and equipment charges)? Are claimed equipment costs submitted in accordance with contractual terms? (See FAR 31.105 concerning allowable equipment costs on covered construction and architect-engineer contracts.)

X. Profit:

S24. Did the contractor provide support for the proposed profit, including identification of the contract clause under which the proposal or claim has been made? (Profit is specifically excluded under the provisions of FAR 52.242-14 and 52.242-17.)

XI. Summary of Adequacy

1. Is the proposal or claim adequate for audit?
  - If yes, proceed with audit and coordinate an acceptable report date with the contracting officer.

- If no, discuss the inadequacies and the corrective actions needed with the contracting officer (and immediately recommend that the contracting officer reject or deny the proposal or claim. Confirm the notifications in writing (include an explanation of the deficiencies and needed corrective actions) with the contracting officer and contractor.
2. If, after receipt and consideration of the auditor's written notification, the contracting officer does not agree to return the proposal or deny the claim, discuss the reasons with the FAO manager and/or RAM to determine if their assistance is needed in convincing the contracting officer to return the proposal or deny the claim.
  3. If, after FAO Manager and/or RAM involvement with contract administration management, the contracting officer insists that an audit be performed on the inadequate proposal or claim, confirm this in writing and advise the contracting officer that an audit cannot be performed on unsupported items, and as a result, all unsupported items will be questioned and an adverse audit opinion will be expressed on the proposal or claim.



DELAY/DISRUPTION PROPOSAL OR CLAIM

Filed under Changes clause ( ) Disputes clause ( )

Contract No. \_\_\_\_\_

Board of Appeals Case No. \_\_\_\_\_

CHRONOLOGY OF SIGNIFICANT EVENTS

Contractor Name: \_\_\_\_\_ Telephone: \_\_\_\_\_

Outside Preparer: \_\_\_\_\_ Telephone: \_\_\_\_\_

Trial Attorney Name: \_\_\_\_\_ Telephone: \_\_\_\_\_

Date of Contract Award: \_\_\_\_\_ Amount: \_\_\_\_\_

Modifications: Refer to contract brief

Date(s) of alleged abnormal condition(s) - From: \_\_\_\_\_ To: \_\_\_\_\_

Description: (Append copies of concise written description, preferably from within the claim; alternatively prepare and append a summary.)

Performance dates per contract - From: \_\_\_\_\_ To: \_\_\_\_\_

Actual performance dates - From: \_\_\_\_\_ To: \_\_\_\_\_

Date entitlement determined or contracting officer decision rendered: \_\_\_\_\_

Date of certification of the proposal or claim: \_\_\_\_\_

Date audit request received: \_\_\_\_\_

Pertinent Government or Contractor Action:  
(Description/Reference)

Date[illegible]

DELAY/DISRUPTION PROPOSAL OR CLAIM

Contract No. \_\_\_\_\_

CONTRACT BRIEF

Contractor Name and Address:

\_\_\_\_\_  
\_\_\_\_\_  
\_\_\_\_\_

RFP No.: \_\_\_\_\_

Price Proposal Evaluation Assignment No.(s): \_\_\_\_\_

Date of Contract Award: \_\_\_\_\_

Amount: \$ \_\_\_\_\_

Contract Type: Fixed Price\_\_\_ T&M \_\_\_ Cost-type \_\_\_ Other\_\_\_\_\_

Procurement Type: Sealed bid \_\_\_ Competitive Negotiation\_\_\_Sole Source\_\_\_ Other  
\_\_\_\_\_

CAS Coverage: Full \_\_\_\_\_ Modified \_\_\_\_\_ None \_\_\_\_\_

Modifications:

No.	Date	Amount	Perf. Period	No.	Date	Amount	Perf. Period
1	_____	\$_____	_____	5	_____	\$_____	_____
2	_____	\$_____	_____	6	_____	\$_____	_____
3	_____	\$_____	_____	7	_____	\$_____	_____
4	_____	\$_____	_____	8	_____	\$_____	_____

ACO Name andAddress:\_\_\_\_\_  
\_\_\_\_\_  
\_\_\_\_\_

PCO Name and Address:\_\_\_\_\_

Applicable \_\_\_\_\_ Procurement  
Regulations:\_\_\_\_\_

Scope of Work:\_\_\_\_\_

Liquidated Damages? Yes ( ) No ( ) Amount: \$ \_\_\_\_\_ per \_\_\_\_\_

General Provisions (append listing)  
Relevant Special Provisions:

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## LISTING OF FRAUD INDICATORS

Fraud is defined in CAM 4-700 as "any willful or conscious wrongdoing that adversely affects the government's interests." It includes, but is not limited to, acts of cheating or dishonesty, which contribute to a loss or injury to the government. Our attorneys have stated that it is not necessary that the contractor representative who certifies the proposal or claim know that the data furnished are incomplete or inaccurate. It is only necessary that data is available and the proposal or claim was prepared in deliberate ignorance of the data or with a reckless disregard of the truth or falsity of data presented in the proposal or claim. Duplicate counting of any proposal or claim element, including delay days, or a proposal or claim for more direct costs than were incurred, might be deemed fraudulent. If the known facts cause the auditor to have a reasonable belief that significant costs have been improperly included in the proposal or claim, the matter should be referred to the proper authorities.

Examples of the types of activities included in the CAM 4-700 definition follow:

1. Falsification of documents, such as time cards or purchase orders.
2. Charging personal expenses to government contracts.
3. Submission of false claims, such as invoices for services not performed or materials not chargeable to the contract.
4. Intentional mischarging or misallocation of costs.
5. Deceit by suppression of the truth.
6. Acts, such as bribery, corrupt payments, which violate the Foreign Corrupt Practices Act, theft, graft, gratuities, and kickbacks.
7. Any unlawful or fraudulent acts resulting from accounting classification practices that are designed to conceal the true nature of the expenses, such as unallowable costs for advertising, entertainment, etc., being classified as office supplies to avoid detection or the concealment of accounting data comprising a proposed estimating factor, such as a material decrement factor used to reduce proposed material costs.
8. Any attempt or conspiracy to engage in, or use, the above devices.

## I. Labor Fraud Indicators

### A. Indirect to Direct:

1. Reclassification/reorganization of employees from indirect to direct.
2. New cost centers appearing on supporting data.
3. Changes in the labor-charging relationships between certain tasks or types of labor.
4. Decrease in indirect expense pools.
5. Increased production labor hours with no corresponding increases in materials used or units shipped, unless this arises from loss of learning.

### B. Labor Accounting by Funding:

1. Notices that certain work order numbers pertaining to incomplete effort may no longer be charged.
2. Actual hours and dollars consistently at or near budgeted amounts for fixed-price work, especially if reimbursable work varies from, or consistently exceeds budget.
3. Employee timecards completed in advance.
4. Employees submit blank timecards.

### C. Adjusting Journal Entries:

1. Transfers from IR&D or BP costs.
2. Transfers from fixed-price government or commercial work.
3. Transfers to open change orders prior to negotiations.
4. Transfers to any work order number of labor costs incurred before the number was established.
5. Transfers to any type of holding or expense account, except for routine processing in which charges to a nonexistent code are suspended for immediate error correction.

### D. Nonconforming Goods or Workmanship:

Significant increases in charging to a government-reimbursable account may indicate that costs of unallowable rework are being mischarged.

### E. Adjustment of Labor Standards:

1. High labor efficiency (hours, usage) variance.
2. Seemingly unrelated tasks and steps on a statement of work.
3. For similar tasks, relatively higher standard hours on cost reimbursable work.
4. Labor standards not updated when contractor updates its technology.
5. Noncurrent labor standards used to support proposals.
6. No supporting documentation for actual or proposed standards.

7. Variances are always in the same direction (this may indicate obsolete standards; however the propriety of disposition of the variance should be reviewed and the impact of a significant one-way variance should be analyzed.)
8. Duplicate employee identification cards for the same time period.
9. Lack of a clear audit trail to verify the propriety of labor charges.
10. Weak internal controls over adjustment of labor charges.

## II. Materials Fraud Indicators

### A. Material Transfers - Financing Inventory (applies to claims only when the government is financing the contract through progress payments etc.).

1. Transfers from government to commercial contracts.
2. Materials ordered and charged in excess of contract amounts.
3. Billings or claims including actual material costs far in excess of the negotiated material costs.
4. Downward adjustments to materials billings as other costs increase.
5. Transfers via any type of holding or suspense account.

### B. Material Transfers - Material Requirements System

1. Transfers of items previously delivered from ongoing jobs to open work orders.
2. Transfers of items scheduled for delivery in the distant future from ongoing jobs to open work orders.
3. Physical transfers from government to commercial work orders without corresponding accounting transfers.
4. Physical transfers from cost-type to fixed-price government job orders without corresponding accounting transfers.
5. Transfers-out at costs substantially different from the original charge.
6. Mass transfers-out from a government work order, leaving little or no remaining materials or work-in-progress inventory but essentially unchanged labor and ODC charges.

### C. Excess/Residual Inventory and Inventory Write-off

1. No accounting for residual or excess materials.
2. Transfers from prior to current or future work orders.
3. Physical transfers from cost-type to fixed-price government job orders without corresponding accounting transfers.
4. Physical transfers from government to commercial work orders without corresponding accounting transfers.
5. Mass transfers to scrap accounts.
6. Mass transfers to inventory write-off accounts.
7. Transfers to or via any type of holding or suspense account.
8. Poor controls over physical inventories.

9. Unexplained increase in proposed or "actual" over historical scrap factor.
10. Unexplained increase in "actual" over historical inventory write-off.

D. Falsification of Documents

1. Original documentation consistently unavailable for the auditor's review.
2. Consistently poor, illegible copies of supporting documentation.
3. Different supporting documents provided for the same item, with item per/unit prices varying widely for no obvious reason.
4. Repeated instances of the use of estimated costs when actual incurred costs from the accounting records more accurately reflect the contract adjustment for which the Government is liable.

E. Repetitive Bidding of Duplicative Material Costs (direct charging or estimating of materials also included in a rate or factor).

1. Vague terms based on "management's judgment" used to bid units of direct materials.
2. Repetitive noncompliance with disclosed bidding practices.

F. Adjustment of Material Standards

1. High materials quantity (efficiency, usage) variance.
2. Work orders, etc. containing materials charges, which appear to be unrelated to the task.
3. Use of noncurrent materials standards, frequently evidenced by "one-sided" variances (all in the same direction, usually unfavorable).
4. Unavailability of documentation supporting proposed or existing standards.
5. Lack of a clear audit trail to verify the propriety of materials charges.
6. Weak internal controls over adjustments to materials charges.

G. Subcontracts: A significant variance between proposed and negotiated vendor prices.

H. Subcontractor Kickbacks

1. Poor internal controls over purchasing, receiving and/or storing.
2. Lack of separation of duties between purchasing and receiving.
3. Lack of rotation or separation of duties in the purchasing department (buyers not regularly rotated to prevent excessive familiarity with specific vendors).
4. Few or no contractor policies on ethical business practices.
5. Poor enforcement of existing contractor policies on ethical business practices.
6. Purchasing employees apparently living beyond their incomes.
7. Circumvention of established procedures for competition of subcontracts or materials purchases.
8. Failure to award subcontract to the low bidder without adequate technical or other justification.



## WORKSHEETS FOR AUDITING UNABSORBED OVERHEAD USING THE EICHLEAY FORMULA

The following provides an illustration of worksheets for auditing the unabsorbed overhead. Worksheet 1 shows the established Eichleay formula elements that may be used for the audit of unabsorbed overhead. Refer to CAM 12-804.1-4 for a detailed description of the elements. Worksheet 2 may be used to show the contractor's computations. The elements of the formula have been left blank, since the contractor's version of the Eichleay formula elements may differ from those of the established formula. For example, the contractor may base its unabsorbed overhead computations on a modified Eichleay formula (see CAM 12-805.2). The modified formula may include substitute elements in Step 1 of the basic Eichleay formula such as original contract price for "contract billings" and total contract billings for the original contract period for "total contract billings for contract period." Such substitutions for the Eichleay formula elements should be discussed in the notes.

### Worksheet 1 Auditor's Eichleay Formula Computations

Step 1. Fixed Overhead Allocable to the Contract:			
$\frac{\text{Contract Billings}^*}{\text{Total Billings for Contract Period}^{**}}$	X	Total fixed overhead for contract period	= Fixed overhead Allocable to the contract
_____		_____	= _____
<div style="text-align: right; margin-right: 20px;"><u>Notes</u></div>			
Step 2. Daily Contract Fixed Overhead Rate			
$\frac{\text{Fixed overhead allocable to contract}}{\text{Days of performance}}$		= Daily contract fixed overhead rate	
_____	=	_____	
Step 3 Unabsorbed Overhead			
Daily contract fixed overhead rate	X	Number of delay days***	= Unabsorbed overhead
_____	X	_____	_____

Contract billings are contract revenues recognized for the period of actual contract performance (see CAM 12-8042).

\*\* Total billings for contract period are revenues for all contracts (including government and commercial) recognized for the period of actual contract performance including the delay period and any modifications (see CAM 12-8042).

\*\*\* Represents the number of days of extended performance beyond the original or previously revised contract performance completion date related to the government caused delay or suspension (CAM 12-804.4).

Notes: **Worksheet 2**

Contractor's Computation of Unabsorbed Overhead

Step 1. :		Notes	
_____	X _____	= _____	
	- _____	= _____	
_____		_____	
Step 2.			
_____	= _____		
_____	= _____		
Step 3 Unabsorbed Overhead			
_____	X _____	= Unabsorbed overhead	
_____	X _____	= _____	

Notes:

### Presenting the Results of Audit of the Eichleay Formula

The following is a suggested format for showing the results of audit of the contractor's Eichleay formula computations, the determination of credits and replacement work or accelerated work. Refer to CAM 12-806.

Contractor's proposed or claimed Eichleay damages	\$	Questioned
		Costs      Notes
Audit computed Eichleay damages (after adjusting for formula errors (Step 11c(4)))	\$	
Questioned costs due to errors in contractor's computation of Eichleay damages		\$
Credit for fixed overhead on proposed or claimed direct costs or additional work (Step 11c(6)(d))		\$
Net impact of the replacement contract(s) or accelerated work on other contracts not reflected in the Eichleay formula computed damages (Step 11c(7)(d))		\$
Total Questioned Costs		\$

### Steps to Assess the Impact of Replacement or Other Substituted Work on the Eichleay Formula (CAM 12-805.4e)

The following is a suggested format for computing the steps, however, the circumstances of the audit will dictate the number of fiscal years involved, number of contracts, etc. Therefore, the format should be revised to suit the particular circumstance.

**Steps:**

1. Determine the contractor's actual fiscal year fixed cost allocation base for the entire performance period of the delayed contract including when the replacement work or other substituted work was performed (the applicable delay/suspension and/or extension periods). Also, determine the fixed cost allocation base of the replacement contract(s) or other substituted work.

Actual (Fiscal Year)*				
	Contract ____	Contract ____	Contract ____	Total
Total Actual Fixed Cost Allocation Base	\$	\$	\$	\$
Replacement or other substituted work allocation base	\$	\$	\$	\$

Compute for each fiscal year totally or partially covered within the total performance period of the delayed contract. If the total fixed overhead base for all contracts in total is known, information on each contract is not required.

2. Compute the actual fixed overhead costs allocated to the fiscal year fixed cost allocation base(s) for the entire performance period of the delayed contract including when the replacement contract(s) or other substituted work was performed.

The applicable fixed overhead cost rates are computed as follows:

Fixed Allocation Bases				
	FY ____	FY ____	FY ____	Total
Contract ____				
Contract ____				
Contract ____				
(a) Total				

(b) Fixed Overhead:

FY ____	FY ____	FY ____	Total
\$	\$	\$	\$

(c) Actual fixed overhead rates: (b)/(a) \*\*

FY ____	FY ____	FY ____
\$	\$	\$

\*\* The actual fixed overhead rates for the applicable fiscal years may be available such that this computation is not necessary.

- Determine the amount of actual fixed overhead applicable to the replacement contract(s) or other substituted work.

	FY ____	FY ____	FY ____	Total
(d) Fixed Overhead Allocation Base (Step 1)	\$		\$	\$
(c) (Fixed overhead rate (Step 2)				
Fixed overhead allocation (c) x (d)	\$		\$	\$

- Use the audited Eichleay formula damages (Audit Step 11c(5)) Enclosure 5.

Unabsorbed Overhead	\$
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- Determine the billings of the replacement work or accelerated work on other contract(s) incurred during the delay and extended periods using the formula from the total billings element of Step (4).

Billings	\$
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- Remove the replacement contract billings from the total contract billings element of the Eichleay formula and recompute the formula damages.

Total billings (Enclosure 5)	\$
Less: Replacement or accelerated contract billings	\$
Reduced Total Billings	\$

- Recompute the Eichleay formula in Enclosure 5 using the reduced total billings computed in Step (6).

Recomputed Eichleay formula damages (without replacement or accelerated work billings)	\$
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- Compute the impact of the replacement work on Eichleay formula damages.

Eichleay formula computed without replacement or accelerated	\$
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work (Step 7)	
Eichleay formula (as Audited) (Step 4)	-\$
Impact of replacement work or accelerated work reflected in the Eichleay formula computed damages.	\$

9. Compare the actual fixed overhead allocated to the replacement contract or accelerated work (Step 3) to the impact of replacement work reflected in the Eichleay formula computed damages (Step 8). Question any significant differences between the Eichleay formula damages and the amount of the fixed overhead applicable to the replacement contract(s) and other substituted work.

Actual fixed overhead allocated to the replacement or accelerated work (Step 3)	\$
Impact of replacement work or accelerated work reflected in the Eichleay formula computed damages.	-\$
Impact of replacement or accelerated work not reflected in the Eichleay formula damages (Questioned amount)	\$

10. Question the impact of replacement work or other substituted work not reflected in the Eichleay formula damages.

Eichleay formula damages as audited (Step 4)	\$
Questioned costs: Impact of replacement work not reflected in the Eichleay formula damages (Step 9)	-\$
Difference	\$

(Questioned costs should be indicated in Enclosure 6 under " Net impact of the replacement contract(s) not reflected in the Eichleay formula computed damages (CAM 12-805.4)."